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IN THE

Supreme Court of the United States

OCTOBER TERM, 1948

No. 201

UNITED STATES OF AMERICA, *Petitioner*

v.

LEONARD H. CARTER, TRUSTEE OF UNION FABRICS, INC., *Bankrupt*

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

The Solicitor General, on behalf of the United States, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Second Circuit, entered in the above-entitled case on May 25, 1948.

OPINIONS BELOW

The memorandum opinion of the referee in bankruptcy (R. 28) is unreported. The opinion of the District Court (R. 19-25) is reported in 73 F. Supp. 685. The opinion of the Circuit Court of Appeals (R. 41) is reported in 168 F. 2d 272.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on May 25, 1948. (R. 45.) The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether an estate in bankruptcy is liable for interest upon tax claims of the United States for the period from and after the date of the filing of the petition in bankruptcy until the claims are paid.

STATUTE INVOLVED

The pertinent statutory provisions are printed in Appendix A, *infra*, pp. 12-15.

STATEMENT

An involuntary petition in bankruptcy was filed against Union Fabrics, Inc., on December 20, 1939. (R. 4.) The United States and the State of New York filed tax claims, asking for interest to the date of payment of the claims.[1] By notices dated

[1] The claims of the United States were for social security taxes for the years 1936, 1937, 1938 and 1939, income taxes for 1935 and 1936, and a miscellaneous tax for 1935 (R. 20), aggregating $9,865.35 (R. 7). The New York State tax claims were for franchise taxes for 1936, 1937 and 1938 and for unemployment insurance taxes (R. 20), aggregating in all $1,660.92 (R. 7). The amount of interest at the rate of 6 per cent per annum on $11,526.27, the aggregate of the claims of both the United States and the State of New York, from December 20, 1939, to February 6, 1947, the date of the trustee's petition to reopen the proceeding, was $4,930.08. (R. 7.)

July 1 and 2, 1946, the trustee in bankruptcy filed objections to the demands for interest on these claims of the United States and of the State of New York beyond the date of the filing of the petition in bankruptcy. (R. 5.) After consolidated hearings, the referee in bankruptcy, on January 24, 1947, filed separate findings of fact and conclusions of law and on the same day filed a consolidated memorandum overruling the trustee's objections to the allowance of interest to the date of payment on the claims of both the United States and the State of New York, and entered orders to that effect. (R. 5, 26-30.) Thereafter the referee reopened the proceeding for the purpose of hearing a further objection by the trustee, based upon certain alleged equitable considerations, but sustained the objections to this evidence and made an order to that effect. (R. 5-8.) Upon a petition for review, the district judge reversed the orders allowing interest on the tax claims to the date of payment and sustaining objections to the trustee's offer of proof at the rehearing. (R. 14-15, 17-19.) He held that interest on the tax claims of both the United States and the State of New York should be treated in the same manner as interest on other claims and not allowed beyond the date of the filing of the petition. (R. 20-24.) With respect to the evidence offered to explain a long delay in the administration of the estate, he regarded such equitable considerations, if pertinent to the determination, as sufficiently shown by the records of the court to augment other reasons for the denial of such interest. (R. 24-25.)

The court below affirmed the orders of the District Court upon the authority of *Saper* v. *City of*

New York, 168 F. 2d 268,[2] decided the same day, as representing the view of the majority of the five judges, sitting in either the *Saper* case or in the instant case, who considered the issue here involved. (R. 42.) However, two of the three judges, who sat in the instant case, did not agree with the opinion of the other three judges who sat in the *Saper* case nor with the decision of the District Court, but acquiesced in the decision of the court below on this question in the *Saper* case, *supra*, since:

> Such a mode of dealing with the appeal before us will settle the law in this circuit as to the allowance of interest on tax claims unless the Supreme Court should hereafter reach a different conclusion.

Nevertheless, in the opinion below, they considered it advisable to state their personal views which were in accord with those of the First Circuit Court of Appeals in *Davis* v. *Green*, 133 F. 2d 451 (R. 42.)

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding that interest on the tax claims of the United States should be allowed only to the date of the filing of the petition in bankruptcy.

2. In failing to hold that interest on the tax claims of the United States should be allowed after

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[2] For convenience the opinion of the court below in the *Saper* case is printed as Appendix B, *infra*, pp. 16-25.

the date of the filing of the petition in bankruptcy and to the date of the payment of these claims.

3. In affirming the order of the District Court.

REASONS FOR GRANTING THE WRIT

1. The decisions of the court below in the instant case and in *Saper* v. *City of New York*, 168 F. 2d 268 (Appendix B, *infra*, pp. 16-25), upon the authority of which the instant case was decided, are directly in conflict with the decision of the First Circuit Court of Appeals in *Davie* v. *Green*, 133 F. 2d 451. This conflict was conceded in the court below both by the three majority judges who sat in the *Saper* case[3] (Appendix B, *infra*, p. 18) and by the two judges in the minority who wrote the opinion in the instant case[4] (R. 42-43).

In the *Saper* case, the majority of the court below reversed the decision of Judge Coxe in the District Court for the Southern District of New York, *sub nom. In re Spotlight Productions*, 75 F. Supp. 458, whose opinion supported the Government's position here; on the other hand, in the instant case, on the authority of the *Saper* case, the opinion of the District Court by Judge Bright (R. 19-25) was affirmed. Indicating the necessity for the settlement by this Court of the disputed question here involved, Judge Clark,[5] writing for the court

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[3] Judges Learned Hand, Swan and Clark.

[4] Judges Augustus N. Hand and Chase.

[5] Judge Clark was the third judge who sat in the instant case and while concurring in the result (R. 44), did not, of course, join in the opinion below, which, as already stated, expressed the contrary views of Judges Augustus N. Hand and Chase.

below in the *Saper* case, succinctly defined the division in the court below and the conflict of the majority with the decision of the First Circuit Court of Appeals, as follows (Appendix B, *infra*, pp. 17-18):

> The matter has been in dispute and must remain so until settled by the Supreme Court. As will appear, the members of this court are not in accord as to the result to be reached. The court as presently constituted is agreed that Judge Coxe's decision, D. C. S. D. N. Y., 75 F. Supp. 458, should be reversed. His decision, however, was in accord with *Davie v. Green*, 1 Cir., 133 F. 2d 451 (which had reversed a referee and a district judge), and has the support of some other district court opinions, *e.g.*, *In re Flayton*, D. C. E. D. N. Y., 42 F. Supp. 1002; and *cf. In re L. Gandolfi & Co.*, D. C. S. D. N. Y., 42 F. Supp. 706. It is contrary to the decision of Judge Bright in *Re Union Fabrics*, D. C. S. D. N. Y., 73 F. Supp. 685, the appeal from which is decided herewith, with the writer of this opinion alone of the court there sitting in agreement with Judge Bright.

2. Clearly, the question presented is of importance in the administration of the federal bankruptcy and tax laws. Indeed, in the *Saper* case the court below observed (Appendix B, *infra*, p. 17):

> The decision must affect all tax claims in bankruptcy, from those of the federal government to those of any state or subdivision thereof.

Settlement of the question by this Court is plainly in the public interest, since it is likely to be presented in almost every bankruptcy proceeding, including many hundreds now pending, and involves not only tax claims of the Federal Government, but also tax claims of every state or subdivision thereof. Bankruptcy Act of 1898, c. 541, 30 Stat. 544, Sections 57j and n and 64a, as amended (Appendix A, *infra*, pp. 12-15).

3. The decision of the court below is believed to be erroneous and the conflicting decision of the First Circuit Court of Appeals in *Davie* v. *Green*, *supra*, correct. Moreover, the decision below probably conflicts with applicable decisions of this Court. It is generally agreed that in 1924 this Court held, in *United States* v. *Childs*, 266 U. S. 304, though without separate discussion,[6] that claims in bankruptcy for taxes drew interest until paid. (First Circuit in *Davie* v. *Green*, *supra*, and the court below, both in the majority opinion in the *Saper* case (Appendix B, *infra*, p. 19) and the minority opinion in the instant case.) (R. 42-43.) In the *Saper* case, however, the majority of the court below held that Congress, by the Act of June 22, 1938, c. 575, 52 Stat. 840, commonly known as the Chandler Act, changed the prior rule with the consequence that thereafter claims for taxes, like

[6] However, as noted in the opinion below, the question was raised in this Court in the arguments of counsel as reported. (R. 42-43). Indeed, it had been expressly decided in the Government's favor by the court below, in the cited case, *sub nom. In re J. Menist & Co.*, 290 Fed. 947, 949-950 (C. C. A. 2d).

other claims, drew interest only to the date of filing of the petition in bankruptcy." (Appendix B, infra, pp. 20-22.) This change in existing law was not made by Congress expressly, but was inferred by the court below from the fact that by the 1938 amendments taxes were classified as debts within Section 64(a) and were required to be proved and filed under Section 57 in the same manner as the claims of other creditors.

The opposing construction is set forth in detail in the opinion of the First Circuit in *Davis* v. *Green*, *supra*, p. 453, and of Judge A. N. Hand in the instant case. (R. 43-44.) In brief, their position is that when Congress passed the Chandler Act, it made many fundamental changes in the law of bankruptcy, and that if it had wished to change pre-existing law to place claims for taxes on the same footing as other claims with respect to interest, it would have done so by specific enactment and in clear and unmistakable terms.[7]

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[7] Moreover, the decision below turns squarely and solely on construction of the applicable federal statutes as a matter of law, since the alleged equitable considerations referred to in the opinion of the District Court (R. 24-25) did not enter into the *ratio decidendi* of either the majority or the minority opinions.

[8] Moreover, the history of federal revenue legislation indicates that Congress intended interest on tax claims to run against estates held by fiduciaries. Revenue Act of 1924, c. 234, 43 Stat. 253, Section 276(c); Revenue Act of 1926, c. 27, 44 Stat. 9, Section 276(c); 67 Cong. Rec., Part 3, p. 3377; *In re Simon*, 11 F. Supp. 18 (D. Conn.), affirmed on other grounds, 80 F. 2d 81 (C. C. A. 2d); cf. *Saper* v. *City of New York* (Appendix B, *infra*, p. 24, fn. 2).

Further, if so well settled and fundamental an interpretation requires, as contended, alteration on the grounds of policy such as alleged injustice or hardship upon general creditors, relief is not with the courts but with the legislature. Indeed, such an express amendment to the statute was proposed to the Eightieth Congress, passed the House of Representatives on June 8, 1948 (94 Cong. Rec. (D. I.), No. 103, p. 7572), and at the time of recess on June 20 was pending in the Senate Committee on the Judiciary.[3] The Report of the House Committee on the Judiciary, which recommended the amendment, clearly indicates its understanding that the Chandler Act had not changed the rule that tax claims in bankruptcy bear interest until payment, and that a

[3] H. R. 5693, which, so far as here pertinent, provides as follows (94 Cong. Rec. (D. I.), No. 103, p. 7569):

> SEC. 11(a) Subdivision j of section 57 of such act, as amended, is amended to read as follows:
>
> "j. (1) Debts owing to the United States or to any State or any subdivision thereof as a penalty or forfeiture shall not be allowed, except for the amount of the pecuniary loss sustained by the act, transaction, or proceeding out of which the penalty or forfeiture arose, with reasonable and actual costs occasioned thereby and such interest as may have accrued on the amount of such loss up to the date of bankruptcy.
>
> "(2) Except where the estate of the bankrupt is solvent, interest accruing after the date of bankruptcy on taxes legally due and owing to the United States or to any State or any subdivision thereof shall not be allowed."

However, this bill even if passed will not dispose of the controversy involved in the instant case nor in the multitude of other pending bankruptcy proceedings. Thus, the bill proposed (p. 7572):

specific amendment would be necessary to change that rule. H. Rep. No. 2083, 80th Cong., 2d Sess., p. 5.[9]

SEC. 31. Effect of this Amendatory Act: (a) Nothing herein contained shall have the effect to release or extinguish any penalty, forfeiture, or liability incurred under any act or acts of which this act is amendatory.

(b) The provisions of this amendatory act shall govern proceedings so far as practicable and applicable in cases pending when it takes effect; but proceedings in cases then pending to which the provisions of this amendatory act are not applicable shall be disposed of conformably to the provisions of said act approved July 1, 1898, and the acts amendatory thereof and supplementary thereto.

SEC. 32. This amendatory act shall take effect and be in force on and after three months from the date of its approval.

[9] H. Rep. No. 2083, 80th Cong., 2d Sess., p. 5:

The addition of clause (2) in the bill is intended to overrule an obsolete rule as to interest on delinquent tax debts. Interest on general unsecured debts, on unsecured Government debts other than taxes, and on debts entitled to priority under section 64a, is suspended at the date of bankruptcy so that, except in the rare case of a solvent estate, interest is allowable only to such date. (Sec. 63a; *Adams* v. *Napa Cantina Wineries* (C. C. A. 9th Cir.), 36 Am. B. R. (N. S.) 8; *In re Gandolfi & Co., Inc.* (S. D., N. Y.), 51 Am. B. R. (N. S.) 521 (governmental debts and other debts entitled to priority); 3 *Collier on Bankruptcy*, 14th Ed., 1835 *et seq.*; 2 *Remington on Bankruptcy*, 4th Ed., secs. 771, 795). However, interest on delinquent tax debts is allowable to the date of payment (*In re Kallak* (D. C., N. D., 1906), 17 Am. B. R. 414; *In re Ashland Emery and Corundum Co.* (D. C., Mass. 1916), 36 Am. B. R. 194; *In re Clark Realty Co.* (C. C. A., 7th Cir., 1918), 42 Am. B. R. 403; *sub silentio, United States* v. *Childs*, 266 U. S. 304, 307

CONCLUSION

For the foregoing reasons, this petition for a writ of certiorari should be granted.

Respectfully submitted.

PHILIP B. PERLMAN,
Solicitor General.

August, 1948.

(1924), 5 Am. B. R. (N. S.) 5). *Although, under the Chandler Act, a tax debt is required to be proved (sec. 57n) and its order of priority ranks below all administration costs and expenses, wages and costs and expenses of creditors successfully opposing a settlement or discharge, or procuring a conviction for an offense (sec. 64a (1), (2), (3)), thereby rendering obsolete the reasoning in the Kallak case, nevertheless its rule has not been changed, and therefore requires this statutory modification.* * * And on overruling the *Kallak* case see *In re Union Fabrics, Inc.* (S. D., N. Y., 1947), 73 F. Supp. 685, appeal pending. (Italics added.)

APPENDIX A

Bankruptcy Act of 1898, c. 541, 30 Stat. 544:

SEC. 57. PROOF AND ALLOWANCE OF CLAIMS.

* * *

j. [as amended by the Act of June 22, 1938, c. 575, 52 Stat. 840, Sec. 1]: Debts owing to the United States or any State or subdivision thereof as a penalty or forfeiture shall not be allowed, except for the amount of the pecuniary loss sustained by the act, transaction, or proceeding out of which the penalty or forfeiture arose, with reasonable and actual costs occasioned thereby and such interest as may have accrued thereon according to law.

* * *

n. [as amended by the Act of May 27, 1926, c. 406, 44 Stat. 662, Sec. 13; Act of June 22, 1938, c. 575, 52 Stat. 840, Sec. 1] Except as otherwise provided in this Act, all claims provable under this Act, including all claims of the United States and of any State or subdivision thereof, shall be proved and filed in the manner provided in this section. Claims which are not filed within six months after the first date set for the first meeting of creditors shall not be allowed: *Provided, however*, That the court may, upon application before the expiration of such period and for cause shown, grant a reasonable fixed extension of time for the filing of claims by the United States or any State or subdivision thereof: * * *.

(11 U. S. C. 1946 ed., Sec. 93.)

SEC. 64. DEBTS WHICH HAVE PRIORITY. [as amended by the Act of May 27, 1926, c. 406, 44 Stat. 662, Sec. 15; Act of June 22, 1938, c. 575, 52 Stat. 840, Sec. 1; Act of June 28, 1946, c. 512, 60 Stat. 323, Sec. 12]

a. The debts to have priority, in advance of the payment of dividends to creditors, and to be paid in full out of bankrupt estates, and the order of payment, shall be (1) the actual and necessary costs and expenses of preserving the estate subsequent to filing the petition; the fees for the referees' salary fund and for the referees' expense fund; the filing fees paid by creditors in involuntary cases; where property of the bankrupt, transferred or concealed by him either before or after the filing of the petition, shall have been recovered for the benefit of the estate of the bankrupt by the efforts and at the cost and expense of one or more creditors, the reasonable costs and expenses of such recovery; the costs and expenses of administration, including the trustee's expenses in opposing the bankrupt's discharge, the fees and mileage payable to witnesses as now or hereafter provided by the laws of the United States, and one reasonable attorney's fee, for the professional services actually rendered, irrespective of the number of attorneys employed, to the petitioning creditors in involuntary cases and to the bankrupt in voluntary and involuntary cases, as the court may allow; (2) wages, not to exceed $600 to each claimant, which have been earned within three months

before the date of the commencement of the proceeding, due to workmen, servants, clerks, or traveling or city salesmen on salary or commission basis, whole or part time, whether or not selling exclusively for the bankrupt; (3) where the confirmation of an arrangement or wage-earner plan or the bankrupt's discharge has been refused, revoked, or set aside upon the objection and through the efforts and at the cost and expense of one or more creditors, or, where through the efforts and at the cost and expense of one or more creditors, evidence shall have been adduced resulting in the conviction of any person of an offense under this Act, the reasonable costs and expenses of such creditors in obtaining such refusal, revocation, or setting aside, or in adducing such evidence; (4) taxes legally due and owing by the bankrupt to the United States or any State or any subdivision thereof: *Provided,* That no order shall be made for the payment of a tax assessed against any property of the bankrupt in excess of the value of the interest of the bankrupt estate therein as determined by the court: *And provided further,* That, in case any question arises as to the amount or legality of any taxes, such question shall be heard and determined by the court; and (5) debts owing to any person, including the United States, who by the laws of the United States in [sic] entitled to priority, and rent owing to a landlord who is entitled to priority by applicable State law: *Provided, however,* That such priority for rent to a landlord shall be restricted to the rent which

is legally due and owing for the actual use and occupancy of the premises affected, and which accrued within three months before the date of bankruptcy.

(11 U. S. C. 1946 ed., Sec. 104.)

APPENDIX B

Opinion of the court below in *Leonard H. Saper, as Trustee in Bankruptcy of Spotlight Productions, Inc.* v. *The City of New York*, decided May 25, 1948.

Before: L. Hand, Swan and Clark, Circuit Judges.

Appeal from the District Court of the United States for the Southern District of New York.

Petition by Lewis H. Saper, as trustee of Spotlight Productions, Inc., bankrupt, for review of an order of a referee in bankruptcy refusing to expunge the claim of the City of New York against the bankrupt for sales and business taxes and ordering the payment of the claim, together with interest at the rate of one per cent per month until the date of payment. From an order affirming the order of the referee, D.C.S.D.N.Y., 75 F. Supp. 158, the petitioner appeals. Order affirmed as to the principal of the taxes, but reversed as to the interest.

[Names of counsel]

CLARK, *Circuit Judge*:

(1) The first point on this appeal concerns the validity of a claim against an estate in bankruptcy for certain sales and business taxes levied by the City of New York against the bankrupt. The trustee concedes the validity of such taxes as were levied upon the bankrupt's sales of machinery manufactured by it, but contests the tax levied on its

purchases of materials. But, as stated in the opinion below, D.C.S.D.N.Y., 75 F. Supp. 458, this is directly contrary to the law and the rulings under it. It is quite settled that both seller and purchaser may be held liable for the city sales tax, though in fact it is primarily imposed upon the purchaser, who must pay it to the City Treasurer if he has failed to pay it to his vendor. § N41-2.0, subds. e, f, of the Administrative Code, New York City. *Kesbeck, Inc. v. McGoldrick*, 278 N. Y. 293, 297, 16 N. E. 2d 288, 119 A. L. R. 536, reargument denied 278 N. Y. 716, 17 N. E. 2d 136; *Fifth Ave Bldg. Co. v. Joseph*, 272 App. Div. 449, 71 N. Y. S. 2d 566; *City of New York v. Feiring*, 313 U. S. 283. The liability of the estate is clear.

(2) The other point, however, the liability of the estate for interest upon these tax claims after bankruptcy and until they are paid, is interesting, important, and difficult. Both the referee and the district court have allowed interest, at the high rate provided by the local code of one per cent per month, so that the accumulating interest is fast approaching the face of the claim.[1] The decision must affect all tax claims in bankruptcy, from those of the federal government to those of any state or subdivision thereof. The matter has been in dis-

[1] The tax period involved as Nov. 1, 1940, to May 31, 1942; the petition in bankruptcy was filed Jan. 5, 1944, and the City's claim originally on May 19, 1944; the referee's order of allowance was made on July 18, 1947. In that order he allowed a sales tax of $495.61, with interest to date of $341.97, and a business tax of $19.72, with interest of $13.13, and made express provision for additional interest at the rate of 1% per month until payment.

pute and must remain so until settled by the Supreme Court. As will appear, the members of this court are not in accord as to the result to be reached. The court as presently constituted is agreed that Judge Coxe's decision, D.C.S.D.N.Y., 75 F. Supp. 458, should be reversed. His decision, however, was in accord with *Davie* v. *Green*, 1 Cir., 133 F. 2d 451 (which had reversed a referee and a district judge), and has the support of some other district court opinions, *e.g.*, *In re Flayton*, D.C.E.D.N.Y., 42 F. Supp. 1002; and *cf. In re L. Gandolfi & Co.*, D.C.S.D.N.Y., 42 F. Supp. 706. It is contrary to the decision of Judge Bright in *Re Union Fabrics*, D.C.S.D.N.Y., 73 F. Supp. 685, the appeal from which is decided herewith,[2] with the writer of this opinion alone of the court there sitting in agreement with Judge Bright. Our decision herein was perhaps somewhat foreshadowed by the remarks of Judge L. Hand in *Hammer* v. *Tuffy*, 2 Cir., 145 F. 2d 447, 449, leaving the question open, and by those of Judge Swan in *United States* v. *Roth*, 2 Cir., 164 F. 2d 575, pointing out that under the recent congressional enactments tax claims were treated substantially as debts of the bankrupt. It is in accord with the views of text writers, notably Messrs. Moore and Oglebay, 3 Collier on Bankruptcy, 14th Ed. 1941, par. 63.16, reiterated in 1946 Cum. Supp. 131, 132, also Mr. Oglebay in 17 J.N.A. Ref. Bankr. 127, 129, 130, 21 *id.* 106, 107, 22 *id.* 41, and the commentator in 61 Harv. L. Rev. 354.

For reasons both of administrative convenience and of fundamental justice and equity it has been

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[2] *Carter* v. *United States et al.*, 2 Cir. 168 F. 2d 274.

steadily held, following the English practice, that interest does not accrue upon claims during the period of bankruptcy administration. *Sexton* v. *Dreyfus*, 219 U. S. 339, 344; *Vanston Bondholders Protective Committee* v. *Green*, 329 U. S. 156, 163, 165; 3 Collier, *loc. cit. supra*.[3] A single exception, that for tax claims, was developed judicially. It appears to have begun with *In re Kallak*, D.C.N.D., 147 F. 276, though the contemporaneous case of *In re William F. Fisher & Co.*, D.C.N.J., 148 F. 907, held to the contrary. But the *Kallak* case set the pattern and was followed by other cases, including *In re J. Menist & Co.*, 2 Cir., 290 F. 947, which, however, allowed interest only at the legal rate. When the Supreme Court reversed this holding to allow interest at the statutory rate, though without separate discussion of our particular problem, *United States* v. *Childs*, 1924, 266 U. S. 304, the matter was considered settled. The reason for the rule was that the original Bankruptcy Act treated tax claims quite differently from other debts; instead of requiring their presentation in due course, it provided that "the court shall order the trustee to pay all taxes legally due and owing by the bankrupt to the United States, State, county, district, or municipality, in advance of the payment of dividends to creditors." § 64a, 11 U. S. C. A. § 104 (a) (before amendment). Hence the trustee was, in effect, compelled to search them out. So taxes were

[3] If, however, a sufficiency of assets develops, the claims will bear interest; and though the usual rule applies also to secured claims, yet where the security itself yields interest or dividends, those are applicable to interest on the claims. 3 Collier, *loc. cit. supra*.

in altogether a separate class; they were to be paid before any administration of the estate, properly speaking, and thus had an absolute priority over the bankrupt's debts. In view of this peculiarly favored position, the like result as to interest was certainly not unnatural, even if not compelled.

In 1926, however, § 64a was amended, by adding the words "in the order of priority as set forth in paragraph (b)"; and of the seven priorities provided in (b), taxes came sixth or next to the last. Even that change might have been considered sufficient to reduce taxes to the status of debts in view of the obvious doubt as to the payment of interest upon a sixth claim in a series where the earlier five admittedly carried none. Moreover, § 64b spoke of the debts "to have priority" in advance of the payment of dividends to creditors, "and to be paid in full out of bankrupt estates," in the order then stated; it was at least odd to think that a wage claim up to $600 was "paid in full" when paid without interest, whereas a tax claim of later priority was not so paid until interest of 12 per cent or more was included.[4] But the issue did not come before the Supreme Court; and apparently the lower federal courts continued their former practice. *Cf. Horn* v. *Boone County, Neb.*, 8 Cir., 44 F. 2d 920; *In re Semon*, D. C. Conn., 11 F. Supp. 18, modified on other grounds, 2 Cir., 80 F. 2d 81.

At any rate the process of assimilation of tax claims to other debts appears, to us at least, to have been completed by the Chandler amendments of

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[4] For the meaning of "paid in full" as limited to the principal, see *Hammer* v. *Tuffy*, *supra*, 145 F. 2d at page 449.

1938. Indeed we thus described the changes in *United States ex. Roth, supra*, 164 F. 2d at pages 577, 578: "By the 1938 amendments, however, taxes were classified as 'debts' within section 64, sub. a, 11 U.S.C.A. § 104, sub. a, and section 57, sub. n, 11 U.S.C.A. § 93, sub. n, was broadened to include 'all claims of the United States' and require them to 'be proved and filed in the manner provided in this section.'[3] Subdivision a of section 57, 11 U.S.C.A. § 93, sub. a, provides that a proof of claim shall state among other matters 'that the claim is justly owing from the bankrupt to the creditor'; * * * Thus it is apparent that the Act, as it now stands, treats the tax claim as a debt and the United States as a creditor which, like other creditors, must make proof of claim on a form" prescribed by the Supreme Court. This, then, took from tax claims their former favored position where no proof or other governmental action was necessary for their enforcement. Thenceforth they must be proved, or otherwise be barred, just like other debts of the bankrupt.

We see no reason to suppose that this did not place tax claims in the same situation as other debts

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[3] In addition, by these amendments the priority subdivision formerly § 64b became § 64a, and the classes of priorities were changed to five instead of seven, the status of tax claims being still next to the last or (4) instead of (6). This was no advancement in position, since former classes (1), (2), and (3) were combined with (1). In 1946, there was added to (1) "the fees for the referees' salary fund and for the referees' expense fund." [This note is not a part of the quotation.]

with respect to interest also.[6] The chief ground taken in *Davis v. Green*, *supra*, and the other cases which argue for the priority of interest, as well as principal, though conceding its inequity, is that Congress by failing to exclude it has re-enacted the old rule. It is dubious at best to rely upon such congressional adoption where "a close scrutiny of the various reports and hearings on the Chandler Act or its predecessor bills reveals nothing to indicate that the problem was ever under consideration." 3 Collier on Bankruptcy, 1946 Cum. Supp., at n. 28a of par. 63.16; 61 Harv. L. Rev. 354. But it is submitted with deference that the pinch is on the other foot. When Congress provided that taxes must be proven like other debts and put them in, and well down in, a hierarchy of other claims, none of which bore interest, we think that like treatment was intended unless some specific exception was stated. This seems all the more likely when we recall the dubious and uncertain history of the original judicial exception.

This conclusion seems to us fortified by arguments of practicality and convenience—if not of equity, as stressed by Judge Bright—which would naturally appeal to legislators or draftsmen, if a

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[6] By making a tax claim a debt of the bankrupt it is brought within the terms of § 63a, 11 U. S. C. A. § 103 (a), defining provable debts, of which subd. (1) allows interest only up to the filing of the petition, and subd. (5) includes provable debts reduced to judgment after filing, but less costs incurred and interest after the filing. Hence under subd. (5), when a tax claim is reduced to judgment after the filing, interest must be deducted. This points up the anomaly of another rule for tax claims not reduced to judgment.

careful exploration of the subject is to be attributed to them. Of course, the allowance of accruing interest to these various state and governmental units "would necessitate constant rescheduling and recomputation of dividends available." 61 Harv. L. Rev. 354, 355. And the net result will be to promote tax claims beyond what seems the clear intent of the statute.[7] Moreover, with the very heavy interest rates now collected by states and municipalities and upheld in *Meilink* v. *Unemployment Reserves Commission of State of California*, 314 U. S. 564, it is apparent that any bankrupt estate whose settlement is delayed for any period of time is likely to be eaten up by the accruing interest on the various taxes now levied against business enterprises. As Referee Hunt points out, 17 J. N. A. Ref. Bankr. 121, 122, no trustee can afford to resist any tax claims, even with proper defenses. With interest accruing thus rapidly, he must settle at once and stop the increase in amount. True, it is suggested that this will be a boon to failing debtors who otherwise might be forced to the wall by rapacious tax collectors driven to precipitous action because the claims do not bear interest. But this is based upon an assumption both of alertness upon

[7] Assume a bankrupt to owe $1,000 to an employee for wages, $1,000 each to three taxing authorities, and $1,000 for rent given priority under state law. Under § 64a, which gives priority to the amount of $600 for wages and allows the others in order, these would be all paid in full if the assets were $5,000 and there were no other general claims beyond the $400 balance on the wage claim. But with interest allowed on the tax claims at 12% (or, perhaps more) per annum during the bankruptcy, possible payments on the later claims would diminish in size as rapidly as Alice in Wonderland.

the part of taxing officials and of the importance of this lone item in the tax structure of municipalities and the state and federal governments which seems to us to have little connection with reality.

Two further arguments of claimants must be noted. One is as to § 57j, an old provision of the law stating that debts owing the United States or any State or subdivision thereof as a penalty or forfeiture shall not be allowed, except for the amount of the pecuniary loss sustained "and such interest as may have accrued thereon according to law." Whether this has any meaning beyond the penalty or forfeiture cases we do not need to consider, for it seems clearly to be operable only *after* the question as to what, if any, interest is legal has been decided.[8] The other is that, since tax claims, if unpaid, are not discharged in bankruptcy, then the unpaid interest on tax claims will survive against the bankrupt even after payment of the tax claims themselves. No cases appear yet to have held that interest thus survives beyond the principal claim which gives it birth. But assuming *arguendo* that interest is not discharged upon payment of the tax claim, we do not see how that fact can be decisive on the present issue. When the Chandler Act was

[8] In the companion case, the United States devotes much attention to various of the federal revenue laws and congressional debates as to changes in them with respect to interest against estates held by fiduciaries. But these do not offer any clear-cut solutions in themselves and are hardly available to change the stated priorities of a bankruptcy act. Obviously the intent of the latter is to treat federal, state and municipal tax claims alike; it would be quite improper to accord the former alone some advantage based upon some newly discovered other federal law or regulation.

under consideration, the House bill made taxes dischargeable, while the Senate amendment retained existing law. Sen. Rep. No. 1916, 75th Cong., 3d Sess., 4, stated that the committee felt "that if Federal taxes were made dischargeable, it would open the door to evasion. The Treasury Department recommended against the House amendment." Thus this was done to protect the revenue, and consideration for, or against, the bankrupt was not an issue. The fact that the bankrupt may not have received an immunity he might desire is not ground for upsetting the statutory scheme of distribution of the estate in the hands of the trustee. The point is academic here, as it will often be—since the bankrupt is a corporation whose existence will be brought to an end by the bankruptcy.

Accordingly the order on appeal will be affirmed to the extent that it refuses to expunge the tax claims, but will be reversed so far as it allows interest after the filing of the petition on January 5, 1944.

Order affirmed in part and reversed in part.

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